

**DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 06-0285
Sales/Use Tax and Penalty
For the Years 2003-2005**

NOTICE: Under IC § 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Sales Tax—Exemption Certificates

Authority: IC § 6-2.5-3-7; IC § 6-2.5-8-8.

Taxpayer protests the imposition of sales tax. Taxpayer claims that it made sales to customer who presented exemption certificates or who otherwise used items sold in a use-tax-exempt manner.

II. Use Tax—Imposition and Methodology

Authority: IC § 6-2.5-3-2; IC § 6-2.5-4-6; IC § 6-2.5-5-8; *Greensburg Motel Assocs., L.P. v. Indiana Dep't of State Revenue*, 629 N.E.2d 1302 (Ind. Tax Ct. 1994); *Indiana Dep't of State Revenue v. Hertz Corp.*, 457 N.E.2d 246 (Ind. Ct. App. 1983); Sales Tax Information Bulletin 60 (July 2006).

Taxpayer protests the assessment of use tax on several items. Taxpayer also protests the inclusion of several accounts in a taxable purchase projection.

III. Tax Administration—Negligence Penalty

Authority: IC § 6-8.1-10-2.1; 45 IAC 15-11-2.

Taxpayer protests the assessment of a negligence penalty.

STATEMENT OF FACTS

Taxpayer is a retailer of semi-trucks and delivery vans. Taxpayer also operates a repair shop, where Taxpayer repairs trucks and sells repair parts.

The Department conducted an audit of Taxpayer for the years 2003 to 2005. The Department and Taxpayer agreed to use a sample of Taxpayer's sales and purchases to determine Taxpayer's additional sales and use tax liability. The Department determined that Taxpayer did not collect sales tax on several customer purchases and did not receive exemption certificates from those

customers. Pursuant to a sampling methodology, the Department assessed Taxpayer additional sales tax.

In addition, the Department reviewed several purchases made by Taxpayer, and assessed use tax. The Department used a sample of Taxpayer's non-capital purchases for the taxable period. The Department then determined the taxable transactions within the total sampled purchases, calculated the percentage of taxable purchases, and applied the percentage to Taxpayer's overall purchases. Taxpayer protested the taxability of sampled individual items. In addition, Taxpayer protested the inclusion of several accounts as part of the sample.

Taxpayer also protested the imposition of a ten percent penalty. The Department conducted a hearing, and this Letter of Findings results. Any determinations not otherwise discussed in this Letter of Findings are considered to be resolved in the manner determined by the Department's audit.

I. Sales Tax—Exemption Certificates

DISCUSSION

Taxpayer's first point of contention is with respect to several items that Taxpayer sold but did not collect sales tax. Taxpayer argues that the customers provided exemption certificates or were in fact using the property sold by Taxpayer for exempt purposes.

Under IC § 6-2.5-3-7,

(a) A person who acquires tangible personal property from a retail merchant for delivery in Indiana is presumed to have acquired the property for storage, use, or consumption in Indiana, unless the person or the retail merchant can produce evidence to rebut that presumption.

(b) A retail merchant is not required to produce evidence of nontaxability under subsection (a) if the retail merchant receives from the person who acquired the property an exemption certificate which certifies, in the form prescribed by the department, that the acquisition is exempt from the use tax.

The section provides a two-prong test for retail merchants with respect to their sales tax collection responsibilities. First, a retail merchant's duty to collect sales/use tax ends when it receives an exemption certificate from a customer. *See also* IC § 6-2.5-8-8(a).

Second, if a customer does not present an exemption certificate to the retail merchant, the retail merchant is required to prove the customer's exempt use of the tangible personal property. In practical terms, the retail merchant is strictly liable for sales tax on a sale of tangible personal property unless it can prove the customer's exempt use of that tangible personal property.

With respect to several customers, Taxpayer provided exemption certificates that it had on file at the time those customers purchased items. Taxpayer is sustained with respect to these customers. With respect to the customers which did not provide exemption certificates at the

point of purchase, Taxpayer has substantiated that the customers used the property in a use-tax exempt manner. Therefore, Taxpayer is sustained with respect to these additional customers.

FINDING

Taxpayer's protest is sustained.

II. Use Tax—Imposition and Methodology

DISCUSSION

Taxpayer disagrees with the Department's conclusion that three specific items were subject to use tax. The first item was a long-distance telephone charge. Taxpayer argues that the telephone charge applied to an interstate telephone charge not subject to sales or use tax under IC § 6-2.5-4-6(b). Taxpayer has provided sufficient information to conclude that the long-distance telephone charge was not subject to use tax.

The second item was a contract for the installation of an item of equipment. The equipment became part of Taxpayer's real property. Taxpayer argues that the installation and equipment contract was a "lump-sum" contract—i.e., all materials and labor appear as one price rather than as separately stated charges. Therefore, Taxpayer argues that the contractor bore the responsibility for paying sales tax on the equipment and Taxpayer should not be subject to use tax on the equipment under IC § 6-2.5-3-2(c) and Sales Tax Information Bulletin 60 (July 2006).

Under IC § 6-2.5-3-2(c),

The use tax is imposed on the addition of tangible personal property to a structure or facility, if, after its addition, the property becomes part of the real estate on which the structure or facility is located. However, the use tax does not apply to additions of tangible personal property described in this subsection, if:

- (1) the state gross retail or use tax has been previously imposed on the sale or use of that property; or
- (2) the ultimate purchaser or recipient of that property would have been exempt from the state gross retail and use taxes if that purchaser or recipient had directly purchased the property from the supplier for addition to the structure or facility.

Sales Tax Information Bulletin 60 (July 2006) discusses the contractor's responsibilities for paying sales or use tax with respect to purchases of tangible personal property subsequently incorporated into real property. Though the July 2006 information bulletin replaced a prior version, the discussion relevant to this protest is substantively unchanged.

With respect to this issue, Taxpayer has provided sufficient information to conclude that Taxpayer correctly treated the contract as not subject to use tax.

The third item challenged was use tax imposed on diesel fuel. Taxpayer purchased the diesel fuel and filled the gas tanks of the trucks sold by Taxpayer. Taxpayer argues that it resold the

diesel fuel when it sold the trucks containing the diesel fuel. Further, Taxpayer argues that it used different vendors for the diesel fuel used in Taxpayer's trucks for resale and Taxpayer's vehicle used in its own day-to-day business.

IC § 6-2.5-5-8 provides an exemption for tangible personal property resold by a retail merchant in the ordinary course of the retail merchant's business. The issue is whether Taxpayer in fact resold the diesel fuel in question.

In *Greensburg Motel Assocs., L.P. v. Indiana Dep't of State Revenue*, 629 N.E.2d 1302 (Ind. Tax Ct. 1994), the court considered the scope of the resale exemption for certain tangible personal property. In *Greensburg Motel*, a motel filed a claim for refund for sales tax paid with respect to tangible personal property used and consumed in its motel rooms. The motel argued that the tangible personal property was purchased for resale to the motel's customers. The court, noting that the tangible personal property was incidental to the rental of motel rooms and the lack of negotiation regarding tangible personal property, held that the motel did not purchase the tangible personal property for resale, and denied the motel's claim for refund. *Id.* at 1305-1306.

The court in *Greensburg Motel* contrasted its case with *Indiana Dep't of State Revenue v. Hertz Corp.*, 457 N.E.2d 246 (Ind. Ct. App. 1983) noting, "In [Hertz], the court held bulk purchases of fuel by an automobile lessor were exempt from sales tax as purchases for resale to lessees. Hertz purchased the gasoline and without changing the form of the gasoline gave the lessees the option to purchase its gasoline." *Greensburg Motel*, 629 N.E.2d at 1305 (internal citations omitted).

When Taxpayer fills the vehicles with fuel, the fuel is incidental to the purchase of the vehicle. The fuel is similar to the tangible personal property in *Greensburg Motel* which was incidental to the provision of a motel room and not separately negotiated from the motel room price. The customer does not separately negotiate or pay a charge with respect to the fuel placed into the customer's vehicle. Accordingly, Taxpayer's protest is denied.

Taxpayer also challenges the methodology used for the use tax audit. In particular, Taxpayer asserted that several accounts used in the projection did not contain purchases subject to use tax per the terms of the projection agreement. Taxpayer has provided sufficient information to substantiate this contention and therefore is sustained with respect to the removal of the accounts specified by Taxpayer in its correspondence, except for any accounts which otherwise include fuel tax.

FINDING

Taxpayer's protest is sustained with respect to the long-distance telephone charges and installation contract. Taxpayer's protest is denied with respect to the diesel fuel purchased and placed into the vehicles that it resold. Taxpayer's protest is sustained in part and denied in part with respect to the accounts used in the projection methodology.

III. Tax Administration--Negligence Penalty

DISCUSSION

The Department may impose a ten (10) percent negligence penalty. IC § 6-8.1-10-2.1 and 45 IAC 15-11-2. Taxpayer's failure to pay the proper amount due as determined by Department audit, generally, will result in penalty assessment. IC § 6-8.1-10-2.1(a)(3). The Department, however, may waive this penalty if the taxpayer can establish that its failure to file "was due to reasonable cause and not due to negligence." 45 IAC 15-11-2(c). A taxpayer may demonstrate reasonable cause by showing "that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed. . . ." *Id.*

Taxpayer has provided sufficient information to conclude that it acted with ordinary business care in its tax duties. Thus, the Department grants Taxpayer's request for penalty waiver.

FINDING

Taxpayer's protest is sustained.

JR/BK/DK May 7, 2007